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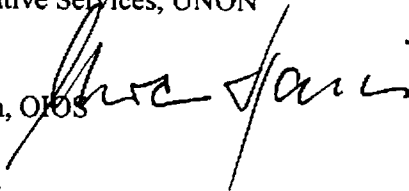
**Internal Audit Division  
Office of Internal Oversight Services**

Reference: AUD: 7-4: 11(0980/03)

24 July 2003

To: Ms. Anna Tibaijuka, Executive Director  
United Nations Human Settlement Programme (UN-Habitat)

Mr. Alexander Barabanov, Chief  
Division of Administrative Services, UNON

From:  Esther Stern, Director  
Internal Audit Division, OIOS 

Subject: **OIOS Audit No. AF2003/93/1: UN-Habitat Settlement Rehabilitation programme (SRP) processing of payments of interim and final invoices for construction contracts**

1. I am pleased to present herewith the final report on the subject audit, which was conducted in Nairobi between March and April 2003. The audit was conducted in accordance with the standards for the professional practice of internal auditing in United Nations organizations
2. The report incorporates, as appropriate, your comments of 17 July 200, which are shown in *italics*. We note with appreciation that you have accepted all 10 recommendations, and that you will implement them by the end of the third quarter 2003. In this regard, we have closed recommendations 03, 04, 05, 06 and 09. We will close recommendations 01, 02, 07, 08 and 10 upon receipt of documentation and clarification as indicated in the text of the report.
3. IAD is also are assessing the overall quality of the audit process and kindly requests that you consult with your managers who dealt directly with the auditor and complete the attached client satisfaction survey form.
4. I take this opportunity to thank management and staff for the assistance and cooperation provided to the auditor in connection with this assignment.

cc: Ms. C. Bertini  
Mr. J. P. Halbwachs  
Board of Auditors  
Programme Officer, OIOS



**United Nations  
OFFICE OF INTERNAL OVERSIGHT SERVICES  
Internal Audit Division**

# **Audit Report**

**Audit subject:** Audit of UN-Habitat SRP processing of invoices for payment

**Audit No. and location:** AF2003/93/1, Nairobi

**Report date:** 24 July 2003

**Audit team:** Nicholas M. Makaa

**UN-Habitat Settlement Rehabilitation Programme (SRP) processing of payments of  
interim and final invoices for construction contracts - AF2003/93/1  
EXECUTIVE SUMMARY**

In March and April 2003, OIOS conducted an audit of UN-Habitat Settlement Rehabilitation programme (SRP) processing of payments of interim and final invoices for construction contracts in Nairobi. The main objective of the audit was to assess the internal control system to ensure its integrity and to examine the achievement of UN-Habitat's objective of processing payments accurately and in a timely manner.

In general, OIOS found that the processing of invoice payment requests was adequate. However, there was a need to strengthen internal controls, and to improve procedures aimed at timely payment of invoices.

**Major findings**

- The integrity and reliability of the Excel database tracking system needed improvement to ensure the completeness and accuracy of data.
- Procedures were needed to handle the bulk receipt of invoices from Iraq and UN-Habitat and to alert the UNON Payments Unit of invoices due for payment processing.
- UN-Habitat has taken steps to process invoices more timely since July 2002. We found however, that although most invoices were processed in a timely manner, it took over 30 workdays in 19 of the 82 invoices tested to process payment requests from receipt of the invoice to when instructions were sent to the bank. There was a delay in processing these invoices in December 2002 due to the lack of resources as most of staff were on leave.
- Procedures should be improved at UN-Habitat Headquarters to randomly verify invoice calculations and to ensure that the field offices check the accuracy of the amounts and adherence to contract terms.
- While efforts have been made toward liquidating the long outstanding balances of unliquidated obligations, steps should be taken to follow up with the field offices to ensure that the remaining \$256,420 in long outstanding unliquidated obligations balances is cleared.
- UN-Habitat in coordination with UNON needs to formalize policy guidance on target milestones for processing all invoice requests for payment including timeframes when the SRP should send requests from Iraq, processing times in each office, and payment target dates.

UN-Habitat needs to streamline the payment process to ensure payment requests are processed within the stipulated contract terms and within 30 days to avoid any risks of late payment penalties arising from failure to make payments according to contract terms.

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## I. INTRODUCTION

1. OIOS conducted an audit of UN-Habitat Settlement Rehabilitation Programme (SRP) processing of payment of interim and final invoices for construction contracts from Northern Iraq in Nairobi. The audit was performed in accordance with general and specific standards for the professional practice of internal auditing in United Nations Organizations.
2. UN-Habitat is one of the nine UN organizations in Northern Iraq implementing projects in various sectors funded under Security Council Resolution (SRC) 986 of 1995. In the Memorandum of Understanding (MOU) between the Secretariat of the UN and the Government of Iraq (GOI) on the implementation of SCR 986, GOI undertook to distribute equitably to the Iraqi population humanitarian supplies purchased with the proceeds of the sale of Iraqi petroleum and petroleum products under the Oil-for-Food programme. The SRP project budget, funded from the 13 percent account, is based on sectoral allocations under the distribution plan approved by the Secretary-General. The allocation of the 13% account to UN-Habitat for phase IX as of 31 December 2002 was \$75.42 million. Its operating costs such as salaries, equipment and supplies, mission travel, mission subsistence allowances, etc. are provided from the 2.2 percent account for administrative expenses. The administrative budget for 2002 was approximately \$18 million, while for 2003 it was about \$17 million.
3. UN-Habitat management's comments on the draft report are reflected in the report as appropriate and are identified in italics.

## II. AUDIT OBJECTIVES

4. The audit objectives were to:
  - (a) Review the internal control system for processing payments of interim and final invoices of the SRP construction contracts to ensure that payments are made accurately and on a timely basis;
  - (b) Substantiate the accuracy of the processes to authorize, verify, record and disburse payments to contractors; and
  - (c) Assess compliance with applicable UN rules and regulations.

## III. AUDIT SCOPE

5. The audit reviewed internal controls in Nairobi for receiving invoices from the field, tracking, processing, making actual cash disbursement, and the timeliness of the process. In addition, support services provided by both UN-Habitat and UNON were reviewed. We examined books and records, documents such as contracts, invoices and supporting documents and requests for payment on a

sample basis from about 3,296 invoices valued at approximately \$204 million which were processed between January 2002 and February 2003. We also interviewed UN-Habitat and UNON staff members.

#### **IV. OVERALL ASSESSMENT**

6. In general, OIOS found that the system to process construction contract invoices was adequate. However, OIOS identified risks including: incomplete or incorrect recording of dates in the Excel database system; lack of formal policy guidance on target milestone dates for processing invoices, inadequate plans to handle bulk receipt of invoices from Iraq and procedures to subsequently alert the Payments Unit of the invoices expected to be processed for payment. Whilst UN-Habitat Headquarters initiated improvement to their system of processing invoices to be timelier since July 2002, there was still some room for improvement.

#### **V. AUDIT FINDINGS AND RECOMMENDATIONS**

##### **A. Receipt of Invoices from Iraq**

7. All incoming mail is logged into a record book by consecutively numbering documents for accountability. We reviewed the system for logging invoices to determine if invoice requests for payment were properly controlled and subsequently entered in the Excel computer database tracking system, and found the following:

- Many requests for invoice payments received from Iraq were recorded in the Excel computer database tracking system with dates different from those recorded in the record book. For example, invoice numbers SUL/CON/367 (3), 430 (4), 397 (4), 385A (4), 331A (5) shown as received and recorded in the record book on 29/1/02 were actually recorded as received on 29/01/01 in the computer tracking system. In addition, invoices numbers SUL/CON/606B (5) and SUL/CON/420 (4) were recorded in the book as received on 19/08/02 while they were recorded in the computer-tracking database as received on 16/8/02. Other invoices did not have receipt date indicated in the computer-tracking table such as SUL/CON/476B (6), but it was recorded as received on 5/9/02 in the book while many other invoices were recorded in the database tracking system but not in the record book such as SUL/CON/334 (F) received on 27/12/02, 166C (4) received on 6/03/03 and 317 (2) received on 6/03/03. This suggests that the database is incomplete and not accurately kept.
- Some invoices were double recorded in the record book while in the tracking system they were properly accounted for as one document. For example, invoice number DHK/CON/384 (5) was recorded as received in the book on 27 May 02 as document number 1719 and 1726 while in the tracking system it was properly recorded as received on the same date.
- The dates of receipt of invoice payment requests were not recorded in the tracking system in

13 items received from Suleimaniyah, 13 items received from Erbil and 4 items received from Dohuk.

- We noted cases where more than one date was recorded for invoices received in Nairobi while in other cases the record indicated the day and month, but not the year, which makes it difficult to determine the actual date when invoices were received from Iraq.

8. These problems demonstrate that the Excel computer database kept for tracking invoice requests for payment from the field is incomplete, lacks integrity, unreliable, and should be corrected.

#### **Recommendation 1**

UN-Habitat should streamline the Excel tracking system for logging invoice requests for payment from Iraq, including improved controls to ensure completeness, accuracy and integrity of the record book and computer tracking system (AF03/93/1/01).

9. *UN-Habitat agreed with this recommendation and indicated that the entire process is being evaluated and efforts are being made to improve the Excel Sheet.* OIOS will close this recommendation in its database upon receipt and review of the revised electronic Excel Tracking Sheet.

#### **B. Planning and monitoring of invoice payment requests from Iraq**

10. UN-Habitat does not effectively plan the processing of bulk invoice requests for payment from Iraq. In addition, it does not solicit from Northern Iraq information regarding invoice payment request plans for the following month or year, which would enable them to prepare for peak invoice payment requests. Furthermore, there is no mechanism to inform UNON's Payments Unit in a timely manner of bulk invoice payment requests. As target dates have not been established, planning to effectively handle invoice requests for payment especially during peak seasons is difficult.

#### **Recommendation 2**

UN-Habitat should develop procedures to periodically obtain invoice requests for payment plans from Iraq to enable UN-Habitat to plan and streamline the processing of invoice payments of contractors (AF03/93/1/02).

11. *UN-Habitat agreed with this recommendation and indicated that appropriate steps will be taken to implement the recommendation by end of July 2003.* OIOS will close this recommendation upon receipt and review of the revised procedures.

### **C. Excel database tracking system**

12. UN-Habitat's Tracking Section logs invoices into an Excel computer database tracking system, which consists of contract number, invoice number, date of receipt from Iraq, date submitted to UNON's Payments Unit, amount of invoice, date sent to bank, confirmation of payment by bank, retention fees, and payment voucher number. The database system is password protected and can only be accessed by UN-Habitat and UNON Payments Unit staff members. Review of the tracking database showed that often-wrong dates had been used or there were no dates to show when invoices were received from Iraq, sent to the Payments Unit, to the Cash Office, or payment instructions sent to the bank. This makes it difficult to track progress in achieving target milestones.

13. In July 2002, a cleansing exercise involving staff members of UN-Habitat and Payments Unit of UNON was carried out that resulted in the elimination of bottlenecks and streamlined controls and timeliness of processing invoice payment requests from Iraq. A subsequent follow up noted that delays were being caused by the field not providing complete information on payment request cover sheets, lack of vendor details, and OBMO/OBPS numbers.

14. We noted that UN-Habitat Headquarters does not randomly verify invoice amount calculations for accuracy, and instead rely on the field offices to check invoice amounts including retention fees. This had resulted in arithmetical inaccuracies. For most of the 82 vouchers reviewed the computation of the invoice total percentage of works executed to date was incorrect. The amount did not reflect the exact invoice amount as a percentage of the total contract value and there were differences sometimes exceeding \$200. In addition, we noted an error in computing the retention fees of invoice contract number SUL/CON/302 (8), which was \$6,521 instead of \$7,298, an understatement of \$777. Furthermore, retention fees for invoice number ERB/CON/00017 were not withheld as required by the contract terms while invoice number DHK/CON/271 had an understatement of \$1,097. In the former case, UN-Habitat explained that the invoice calculations are computed by the computer system used in the field offices.

#### **Recommendations 3 to 4**

UN-Habitat should:

- (i) Instruct field offices to provide complete information on the face sheet of invoice submissions to ensure easy and timely processing at UN-Habitat Headquarters (AF03/93/1/03); and

- (ii) Require that a PMO verify invoice computations and check them against the terms of the contract to ensure invoice amounts are accurate and reasonable as a basis for certification in accordance with functions of certifying officers stipulated in ST/AI/352 and Financial Rule 105.5 (b) as revised (AF03/93/1/04).

15. *UN-Habitat agreed with Recommendations 03 and 04 and indicated that appropriate actions had been taken to implement them.* OIOS is therefore closing these recommendations in its database.

#### **D. Processing of payment vouchers by Payments Unit**

16. After inspection and certification, invoices are forwarded to UNON's Payments Unit. Upon receipt, the Payments Unit checks to ensure a valid obligation has been created in IMIS, whether the payment is valid and due, and that UN-Habitat has inspected and certified the payment. If mistakes, inaccuracies, or inadequate information are noted, instead of returning the document to UN-Habitat, there is an arrangement that the Payments Unit informs UN-Habitat via e-mail of the problem with the payment request. The Approving Officer then approves both manual and electronic records in IMIS. The process from receipt of payment request documents in the Payments Unit to the time they are forwarded to cash office takes 5 workdays.

17. The review of 82 sample vouchers found that:

- (a) All vouchers were made only on the basis of duly certified supporting vouchers and other documents;
- (b) All vouchers except two were properly authorized by the designated approving officer for availability of funds. Two payment vouchers (numbers IMIS document ID # 10814 and 10816) did not bear the signature of the approving officer, which violates the relevant FR and risks of making invalid payments;
- (c) All payments were made by cheque unless exemption had been obtained from the Controller;
- (d) Supporting documents included with the payment vouchers were checked for accuracy and completeness;
- (e) One contract (ERB/CON/00017) for seven invoices totalling \$64,379 had been paid in full without withholding the 10 per cent retention fees of \$6,438 as required by the terms of the contract;
- (f) All invoices were properly certified for funds availability per the new FR 105.4 and 105.5; and

- (g) There were no duplicate payments of invoices in the 82 invoices checked and the cancellation "PAID" was made after processing payment to ensure there were no duplicate payments.

#### **Recommendation 5**

The UNON Cash Office in consultation with the UNON Payments Unit should ensure that the designated approving officer authorizes all hard copies of the payment vouchers including the voucher with IMIS document numbers ID #10814 and 10816 dated 9 January 2003 (AF03/93/1/05).

18. *UN-Habitat agreed with this recommendation and indicated that it will ensure that recommended actions will be implemented.* OIOS is therefore closing this recommendation in the database.

#### **E. Processing of disbursements by Cash Office**

19. The UNON Cash Office is responsible for making disbursements to contractors. The Cash Office takes approximately 2 workdays to process a payment and up to 5 work days to receive confirmation of payment from the bank.

#### **Cash-Flow Statements**

20. While UN-Habitat prepares cash flow statements it does not share these statements with the Cash Office for planning and control purposes. Consequently, the requirements of financial rule 7.082 calling for proper planning and control purposes are not enforced.

#### **Recommendation 6**

UN-Habitat in coordination with the UNON Cash Office should share information on cash flow statements to ensure that problems identified are corrected and to facilitate planning and control. (AF03/93/1/06).

21. *UN-Habitat agreed with this recommendation and indicated that it is now sharing monthly cash projections with both UNON Cash Office and Accounts Section.* OIOS is therefore closing this recommendation in the database.

#### **F. Timeliness of processing invoice requests for payment from Iraq**

22. UN-Habitat has taken the initiative to streamline the processing of invoice requests for

payment received from Iraq. Whilst meeting minutes have identified a general time frame for processing invoices by each office in Nairobi, there is no circular (policy guidance) issued by UN-Habitat that identifies target milestone dates. This has resulted in a lack of accountability for processing invoices and a risk of not processing invoices in a timely manner.

23. UN-Habitat targeted a maximum of 28 working days, from receipt of invoices from the field to the time when instructions are sent to the bank to effect payment. While UN-Habitat uses workdays to monitor progress, general contract clauses state that payments are due within a period ranging from 28 to 30 calendar days. From the sample of 82 invoices tested, it took over 30 workdays in 19 of the items or 23 percent to process payment requests. Consequently, UN-Habitat risks incurring penalty costs due to making late payments to contractors.

24. There is no mechanism in place to collect statistics on the actual time taken to complete different actions. For example, the audit could not confirm whether it takes less than 5 work days to process invoices in the Payments Unit prior to submitting to Cash Office because statistical data is not kept. Such a mechanism would enable UN-Habitat to monitor the achievement of time targets and identify any bottlenecks. A spot check showed that the Excel tracking system used wrong dates while others were incomplete.

#### **Recommendations 7 to 9**

UN-Habitat in coordination with UNON should:

- (i) Issue formal policy guidance on target milestones for processing SRP invoice requests in each office (AF03/93/1/07);
- (ii) Collect statistical data to monitor the timeliness of processing all invoice requests at different stages from when requests are received in Nairobi to when actual payment is made to contractors in order to monitor the achievement of target milestones and identify bottlenecks requiring corrective action (AF03/93/1/08); and
- (iii) Streamline the process to ensure payment requests are processed within the stipulated contract terms with a maximum duration of 30 days to avoid paying penalties (AF03/93/1/09).

25. *UN-Habitat agreed with Recommendation 07 and indicated that guidelines on benchmarks will be formally issued shortly and will include already established practices in UNON. OIOS will close this recommendation upon receipt of the guidelines on benchmarks.*

26. *UN-Habitat agreed with Recommendation 08 and indicated that statistical data will be included in Excel Tracking Sheets as part of Recommendation 01. OIOS will close this*

recommendation in its database upon receipt of the electronic corrected Excel Tracking Sheets with statistical data.

27. *UN-Habitat agreed with Recommendation 09, and indicated that the payment process has been streamlined to an acceptable level of 14 days in Nairobi from the point of receiving the request in UN-Habitat to the payment by UNON. In addition, UN-Habitat stated that since the implementation of this new procedure, it has received positive feed back from Iraq and no complaints from contractors about the payment period. UN-Habitat also noted that it is at no risk of incurring penalties arising from delayed payments as the standard clause in contracts stipulates that "UN-Habitat shall ensure to its best effort to transfer the funds to the bank of the contractor within 28 days of the date of the monthly interim certificate of acceptance". Lastly, it stated that it cannot ensure the 28-day period is guaranteed, but will implement all the measures to comply with the requirement on a best effort basis. OIOS acknowledges UN-Habitat's clarification and is closing this recommendation.*

#### **G. Unliquidated Obligations**

28. Prior to introduction of IMIS at Nairobi in July 2001, a special account (account # UNA 2310) was set up for processing retention payments. As of 30 April 2003, a balance of \$256,420 was outstanding in the account, which should have been gradually liquidated. Whilst efforts had been made to reduce the outstanding balance, more follow up action with field offices is necessary as many outstanding items had last or final payment requests received from Iraq in the years 2000 or 2001.

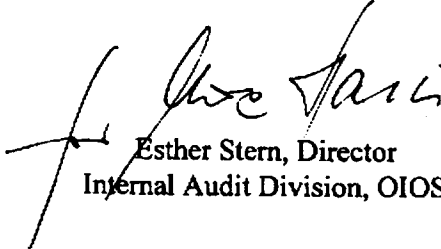
#### **Recommendation 10**

UN-Habitat Headquarters should follow up with field offices in coordination with UNON's Payments Unit to ensure that the \$256,420, outstanding in the special account set up for processing retention payments is liquidated (AF03/93/1/010).

29. *UN-Habitat agreed with this recommendation and indicated that it will continue to work on this account and based on additional information from the field \$256,420 will be reduced to \$128,568 and the remaining balance, which consists of pending retention payments is valid and needs to be kept. OIOS will close this recommendation upon receipt of documentation showing the reduced amount and the pending retention payments that are considered valid.*

## VI. ACKNOWLEDGEMENT

30. We wish to express our appreciation for the assistance and cooperation extended to the audit team by UN-Habitat and UNON.



Esther Stern, Director  
Internal Audit Division, OIOS